

Message Text

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SUBJECT: ROKG-IMF CONSULTATIONS GO SMOOTHLY

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SUMMARY: RECENT ROKG-IMF CONSULTATIONS WENT VERY SMOOTHLY,
WITH THE IMF MISSION REPORTEDLY CONCLUDING THAT KOREA HAS
SO FAR WEATHERED OIL SHOCK AND INTERNATIONAL RECESSION-
RELATED DIFFICULTIES REMARKABLY WELL. THE CONSULTATIONS
WERE GENERAL IN NATURE, WITH NO SPECIFIC AGREEMENTS
NEGOTIATED. THE IMF TEAM WAS GENERALLY PLEASED WITH ROKG
PLANS FOR 1976 ON THE CONDITION THE ROKG DOES, IN FACT,
MAINTAIN ITS RESOLVE TO GIVE TOP PRIORITY TO THE BALANCE OF
PAYMENTS AND INFLATION TARGETS. THE MISSION DID EXPRESS SOME
CONTINUING DISSATISFACTION WITH WEAKNESSES IN ROKG FISCAL
PERFORMANCE AND WITH ITS FAILURE TO TAKE MORE FORCEFUL ACTION TO
RESTORE POSITIVE INTEREST RATES. RESPONDING TO AN EXPRESSION OF
ROKG CONCERN OVER RECENT PROTECTIONIST MEASURES BY ADVANCED
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COUNTRIES, THE MISSION REPORTEDLY INDICATED THE IMF

SHARES THAT CONCERN. TOTAL KOREAN DRAWINGS FROM IMF RESOURCES IN 1976 ARE ANTICIPATED TO BE ROUGHLY \$120 MILLION IN A COMBINATION OF THE EXPANDED FIRST CREDIT TRANCHE, ANOTHER DRAWING UNDER THE OIL CREDIT FACILITY AND LIKELY ROKG ELIGIBILITY UNDER THE COMPENSATORY FINANCING FACILITY. AN IMF MISSION IS EXPECTED TO RETURN IN JUNE TO NEGOTIATE A NEW STANDBY AGREEMENT TO SUCCEED THE CURRENT JULY-TO-JULY AGREEMENT. END SUMMARY

1. AN IMF MISSION HEADED BY JOACHIM AHRENSDORF CONCLUDED TWO WEEKS OF ANNUAL CONSULTATIONS WITH THE ROKG ON FEB. 28. BY ALL ACCOUNTS, THE CONSULTATIONS WENT VERY SMOOTHLY. THIS MAY, IN PART, HAVE BEEN DUE TO THE FACT THERE WAS NO NEED TO COME TO GRIPS WITH SPECIFIC FIGURES. THE ROKG, WHICH HAS OBSERVED ALL MID-POINT (JANUARY 1, 1976) CEILINGS ESTABLISHED IN THE CURRENT JULY-TO-JULY STANDBY AGREEMENT (SEE REF A FOR DETAILS) DID NOT SEEK ANY REVISIONS IN PRESENT FULL-YEAR CEILINGS. (THIS APPARENTLY WAS THE FIRST TIME WITHIN MEMORY THAT HAS HAPPENED.) SOME EXPLORATORY DISCUSSIONS WERE HELD ON POSSIBLE CONDITIONS FOR DRAWINGS UNDER THE EXTENDED FUND FACILITY, BUT THESE WERE VERY GENERAL IN NATURE.

2. WE UNDERSTAND THE MISSION CONCLUDED THAT KOREA HAS WEATHERED THE OIL SHOCK AND INTERNATIONAL RECESSION RELATED DIFFICULTIES OF 1974 AND 1975 REMARKABLY WELL SO FAR. ONE ROKG OFFICIAL WENT SO FAR AS TO EQUATE THE IMF ASSESSMENT WITH OFFICIAL RECOGNITION THAT KOREA HAS SUCCESSFULLY TURNED THE CORNER ON THE BALANCE OF PAYMENTS DIFFICULTIES THAT THREATENED LAST SPRING.

3. THE MISSION COMMENDED THE ROKG ON ITS DECLARED DECISION TO FOCUS 1976 POLICY ON ACHIEVING ITS BALANCE OF PAYMENTS AND INFLATION TARGETS. (SEE REFTEL B, C AND D FOR DETAILS). THE OFFICIAL PLANNING TARGETS WERE GENERALLY FOUND TO BE REALISTIC WITH THE EXCEPTION OF SOME MISGIVINGS THAT THE IMPORT PROJECTION MAY BE UNDERESTIMATED. THE MISSION EMPHASIZED THAT ITS FAVORABLE ASSESSMENT HINGED ON THE ROKG CONTINUING ITS DETERMINATION TO MANAGE DEMAND TO ACCOMMODATE THE SELF-IMPOSED CONSTRAINTS OF ITS BALANCE OF PAYMENTS AND INFLATION TARGETS, WITH DOMESTIC CREDIT POLICY VIEWED AS THE KEY INSTRUMENT.

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4. THE MISSION DID EXPRESS SOME CONCERN OVER THE ROKG'S PROGRESS TO DATE IN DEALING WITH CERTAIN STRUCTURAL PROBLEMS THE IMF, AMONG OTHERS, HAS IDENTIFIED IN THE PAST. THESE RELATE CHIEFLY TO: (1) WEAKNESSES IN FISCAL PERFORMANCE WITH ITS CORRESPONDING IMPACT ON THE LEVEL OF PUBLIC SAVINGS AND INVESTMENT, AND (2) MISALIGNMENT OF CERTAIN RELATIVE PRICES, PARTICULARLY INTEREST RATES, WHICH REDUCED PRIVATE SAVINGS.

5. THE IMF'S CHIEF CONCERN ON THE EXPENDITURE SIDE OF THE FISCAL PROBLEM INVOLVES THE RECENT LARGE DEFICITS IN EXTRABUDGETARY ACCOUNTS. WHICLE PLEASED THAT THE ROKG HAS APPARENTLY ELIMINATED THE FERTILIZER SUBSIDY WITH THE SHARP HIKE IN FERTILIZER PRICES LAST DECEMBER, THE IMF IS CONTINUING TO URGE MORE EFFECTIVE ACTION IN DEALING WITH THE GRAIN MANAGEMENT FUND DEFICIT. ON THE REVENUE SIDE, THE IMF HAS WELCOMED ROKG PLANS TO INTRODUCE A VALUE-ADDED TAX (VAT) IN 1977, BUT WOULD LIKE TO SEE STILL FURTHER REFORMS AIMED AT DEVELOPING A MORE AUTOMATIC RESPONSE IN REVENUE GENERATIONS DURING PERIODS OF INFLATION AND EXCESS DEMAND. WITH REGARD TO INTEREST RATES, THE MISSION CONTINUED TO PRESS FOR MORE DECISIVE ACTION TO RESTORE POSITIVE REAL INTEREST RATES, BOTH FROM THE POINT OF VIEW OF RAISING SAVINGS IN FINANCIAL ASSETS AND AS A MEANS OF DAMPENING INFLATIONARY EXPECTATIONS.

6. ON THE ISSUE OF IMPORT RESTRICTIONS, THE ROKG IS EXPECTED TO ANNOUNCE BY MARCH 31 LIBERALIZATIONS OF IMPORT RESTRICTIONS EQUIVALENT TO THE \$67 MILLION EFFECT OF RESTRICTIONS IMPOSED ON 39 ITEMS LAST APRIL, AS IT PLEDGED TO DO IN THE CURRENT STANDBY. HOWEVER, WITHOUT SINGLING OUT SPECIFIC CASES, THE ROKG ALSO TOOK THE OPPORTUNITY OF THE MISSION'S VISIT TO EXPRESS ITS OWN CONCERN OVER RECENT PROTECTIONIST MEASURES BY ADVANCED COUNTRIES WHICH AFFECT, OR THREATEN TO AFFECT, KOREAN EXPORTS. THE MISSION GSPORTEDLY INDICATED THE IMF SHARES THE ROKG'S CONCERN.

7. THE MISSION BROUGHT SOME GOOD NEWS IN TERMS OF LIKELY AVAILABILITIES OF IMF CREDITS THIS YEAR. WITH NEW FUNDING HAVING BEEN FOUND, THE IMF IS EXPECTED TO AUTHORIZE DRAWING OF ANOTHER TRANCHE UNDER THE IMF OIL CREDIT FACILITY, PROBABLY AMOUNTING TO \$50 TO \$60 MILLION. THE DECISION AT THE IMF INTERIM COMMITTEE MEETING IN JANUARY TO INCREASE STANDBY CREDIT TRANCHES BY 45 LIMITED OFFICIAL USE

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PERCENT TEMPORARILY, PENDING FORMAL APPROVAL OF INCREASES IN IMF QUOTAS, GIVES KOREA AN ADDITIONAL \$11 MILLION FOR ITS FIRST CREDIT TRANCHE WHICH IT WILL PROBABLY DRAW IN JUNE. THE MISSION ALSO INFORMALLY TOLD ROKG OFFICIALS THAT KOREA IS LIKELY TO BE CONSIDERED ELIGIBLE FOR DRAWINGS OF AROUND \$50 MILLION FROM THE COMPENSATORY FINANCING FACILITY THIS YEAR.

IN VIEW OF THE ABOVE, THE ROKG CURRENTLY PLANS NOT TO SEEK FINALIZATION OF AN AGREEMENT FOR DRAWINGS UNDER THE EXTENDED FUND FACILITY UNTIL AFTER THE NEW IMF QUOTAS TAKE EFFECT, WHICH, IN KOREA'S CASE, WILL DOUBLE THE BASE FOR CALCULATING ITS ELIGIBILITY UNDER THAT FACILITY.

8. AN IMF MISSION IS EXPECTED TO RETURN IN JUNE TO NEGOTIATE A NEW STANDBY AGREEMENT.

9. THE EMBASSY'S COMMENTS AND A REVIEW OF CURRENT ECONOMIC
TRENDS ARE BEING FORWARDED BY SEPTTEL.
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